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Foreign Economic Trends and Their Implications for the United States

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Kuwait: Key Economic Indicators
All Values in Millions of U.S. Dollars Unless Otherwise Indicated

Income and Production	1986	1987	1988
GDP at Current Prices	16,567	19,489	20,463E
Per Capita GDP	9,250	10,405	10,371E
Crude Oil Production (million bpd)*	1.4E	1.3E	1.4E
Refinery Throughput (million bbl)	400E	500E	500E
Electric Power (million kwh)	16,934	18,081	19,730
Desalinated Water (million imp gal)	38,712	40,552	40,946
Population (thousands)	1,791	1,873	1,958
Money and Prices			
Money Supply (M1)	3,172	3,491	3,198
Quasi Money (M2-M1)	12,522	13,600	15,057
Wholesale Price Index (1980=100)	107.5	111.1	116.2
Consumer Price Index (1978=100)	143.8	144.7	146.9
Exchange Rate: 1 Kuwaiti Dinar	$3.44	$3.586	$3.585
Balance of Payments			
Exports and Reexports	7,231	8,355	8,100E
of which, Oil	6,378	7,520	7,000E
Imports (CIF)	5,893	5,293	6,100E
Trade Surplus	1,338	3,062	2,000E
Current Account Surplus	6,161	4,410	4,000E
U.S. Exports to Kuwait	656.6	504.6	690
U.S. Imports from Kuwait	307.1	568.6	464
U.S. Trade Balance with Kuwait	349.5	-64.0	226
Public Finance (FY runs June-July)	87/88 (Actual)	88/89 (Budget)	89/90 (Budget)
Oil Revenues	7,176	6,249	6,551
Non-Oil Revenues	938	926	971
Book Revenues	8,114	7,175	7,522
Current and Development Expenditures	10,110	11,160	11,219
Current Expenditures	8,113	8,512	8,655
Land and Development	1,997	2,648	2,564
Fund for Future Generations	811	717	752
Total Outlays	10,921	11,877	11,971
Book Deficit	2,807	4,702	4,449

E - Embassy Estimate
* - Includes Kuwait share of Neutral Zone production
Sources: Central Bank of Kuwait: Quarterly Statistical Bulletin
Ministry of Planning: Monthly Digest of Statistics
Official Gazette
U.S. trade statistics: U.S. Department of Commerce

SUMMARY

The Kuwaiti economy grew an estimated 5 percent in 1988. The second year of renewed expansion after a long economic contraction saw increased output in both the oil and non-oil sectors. Expansionary monetary and fiscal policies helped fuel the expansion, although the wide variations in oil prices over the year introduced uncertainty about the contribution of the oil sector to future economic expansion. Kuwait has remained an economy open to foreign trade and payments flows, although the traditional markets for reexports to Iran and Iraq have been depressed for most of the past decade due to the war. The cease-fire in the Iran/Iraq war has not yet sparked the renewal of the reexport trade that many Kuwaiti observers had expected. The Kuwaiti Government budget has remained stable at an expenditure level of around $10.5 billion for the past several years with an effective control over outlays despite the economic retrenchment of the mid-1980s. The government's program of financing the state budget deficit through the sale of bonds has continued to be successful. Monetary policy has tightened up after the previous policy of encouraging low interest rates led to a drain on foreign currency holdings of the Central Bank. With the increase in interest rates in December 1988, new investment outside the oil industry will be increasingly unlikely.

The banking sector in Kuwait enjoyed a good year, for the most part, in 1988. The Central Bank continues to administer the so-called Difficult Settlements Program, which provides support to those commercial banks with a large portfolio of bad domestic debt left from the Kuwaiti financial crisis of the early 1980s. The inflation rate in Kuwait remained very low with the Kuwaiti market basket showing little change in prices. The foreign trade account remained in surplus, although at a somewhat lower level than in previous years, but the Embassy estimates that the balance-of-payments current account remained at about the $4.0 billion surplus level.

With proven oil reserves of more than 90 billion barrels, Kuwait will remain a major oil producer well into the next century. Kuwait was a founding member of OPEC, and its quota as of December 1988 was a little over 1 million barrels per day. The Kuwaiti Government has indicated, however, that it will produce oil at a rate of at least 1.35 million barrels per day. The Kuwait Petroleum Corporation, the government-owned corporation which is responsible for producing and marketing Kuwait's oil, has invested several billion dollars in establishing an oil refinery network in Kuwait, and Kuwait can now export upwards of 700,000 barrels of oil per day from its three domestic refineries. Kuwait also has a retail oil distribution network abroad, mainly concentrated in Western Europe.

Moderate economic growth rates in Kuwait should provide an expanding market for U.S. growth rates. A competitive exchange rate for the dollar has also boosted prospects for U.S. exporters in recent years, as the United States has nearly drawn equal with Japan as the top supplier to the local market. The government budget remains the main engine of domestic business activity, as the cease-fire in the Gulf War has yet to generate much Kuwait-based business. Government spending will target essential services in the areas of housing, road construction, public utilities, education, telecommunications, and medical care. U.S. firms do well in areas where U.S. products have an edge in technology and price in this very price-conscious market. Kuwaiti adherence to the Arab League boycott of Israel may prevent some U.S. firms from doing business in Kuwait. To penetrate the local market, a local agent or representative is usually required, and U.S. firms should seek professional advice to understand the application of Kuwaiti corporate tax law.

PART A: CURRENT ECONOMIC SITUATION AND TRENDS

Economic Growth: The Kuwaiti economy enjoyed another year of economic growth in 1988, with most estimates of the gross domestic product (GDP) growth rate centering around 5 percent. The variation in oil sector GDP is much wider than the non-oil GDP. Over the past decade the oil sector GDP has declined, and this has had an effect on economic activity. The oil sector had its ups and downs during 1988 because of the swings in the world oil market. Nevertheless, the second year of moderate total GDP growth has increased confidence that the economy is on the rebound after being in recession for the first half of the decade. In the early 1980s, Kuwait suffered a banking and financial crisis following the crash of the Kuwait-based Al Manakh stock market after a wild bout of speculation. With the banking crisis mostly resolved, the Kuwaiti Government has attempted to get the economy going again through expansionary monetary and fiscal policies.

Kuwait's development policies have emphasized a reliance on Kuwait's petroleum resources and the mercantile skills of the commercial and banking establishment. Kuwait has few restrictions on trade or financial flows. There also has been considerable government sector expansion in social services, for example in medical care, where the government feels the private sector is not providing sufficient service. The Kuwaiti Government has also made major investments in infrastructure development. At the same time, Kuwait has placed great reliance on the private sector to develop the economy. Providing that the cease-fire in the Iran/Iraq war continues, overall uncertainty surrounding economic decision-making will decrease.

Kuwait exports its oil by shipping it in tankers since there are no pipelines connecting Kuwaiti oil fields with non-Kuwaiti export terminals. When Kuwait's oil exports were threatened during the latter part of the Iran/Iraq war, the maritime protection regime, maintained by U.S. naval forces protecting Kuwaiti-owned ships flying the U.S. flag, guaranteed Kuwait's ability to supply its customers. Even with the return to economic growth and the confidence building atmosphere of the cease-fire, Kuwait's economy is producing at levels below those of the early 1980s. The Kuwaiti authorities hope to continue modest growth rates of recent years, although at the end of 1988 they had to tighten up the relaxed monetary policy which prevailed in recent years.

Fiscal Policy: The Kuwaiti Government in recent years has followed a policy of maintaining expenditure levels at around Kuwaiti dinar (KD) 3 billion ($10.5 billion, approximately). The fiscal year which ended in June 1988 was no exception, with outlays falling short of the budgeted KD3.2 billion to reach only KD2.8 billion. The Finance Ministry expected to spend KD3.195 billion in the fiscal year which began in July 1988, and it is expected to boost expenditures further in the fiscal year beginning in July 1989. Even though budget increases have been announced, it is not at all clear that the expenditures actually made will reach the projected levels. The Government of Kuwait in recent years has repeatedly under-spent its budget. The budget's area of greatest impact on the pace of domestic economic expansion has been the construction sector. However, with the conclusion of a number of major projects in recent years, the budget has had less of a stimulative effect on the economy. The government nevertheless has remained active in the residential construction and highway construction fields, and major project spending should pick up in coming years.

The Finance Ministry has continued to set aside funding for the Reserve Fund For Future Generations (RFFG). According to government policy since 1976, 10 percent of ordinary revenues are set aside each year as the govenment's new allocation to the RFFG assets. The RFFG is destined to provide a legacy to the Kuwaiti generations of the 21st century, and it is not to be drawn on until after the turn of the century. The funding is treated as a commitment outside the ordinary budget process, and the outlays into the fund have no effect on fiscal policy.

On the revenue side, the government collects more than 85 percent of its income from oil and gas sales by the state-owned Kuwait Petroleum Corporation. The Kuwaiti Government has been conservative in its revenue estimates, and the 1987/88 fiscal year revenues surpassed original estimates by KD273 million, or close to $1 billion. Kuwait has no personal income tax and collects only a modest amount of revenues from tariffs and charges on government services. Although there has been some discussion of increasing fees for state-provided services, no significant changes are expected in the way the Kuwaiti Government collects its income.

The budget for the fiscal year which began in July 1988 calls for income of KD2.056 billion, another conservative estimate of income. Although the authorities have projected a deficit for FY 1988/89 of over KD1.1 billion, the actual deficit is likely to be significantly less than KD1 billion. This deficit does not take into account the income the government earns on its investments. If the income were included, it would almost certainly cover the deficit.

The Kuwaiti authorities have decided to continue the practice began in November 1987 of covering the deficit in the ordinary budget by issuing treasury bills and bonds. The ordinary budget does not include investment income. The debt limit for the issuance of the bills and the longer term notes has been set at KD3 billion, or about $10.5 billion. The purpose of the deficit funding scheme is partly to allow the Finance Ministry to run the deficit in the ordinary budget without having to draw down funds in the State General Reserve and partly to give the monetary authorities another instrument of monetary policy.

Monetary Policy: The Central Bank of Kuwait maintained its expansionary monetary policy throughout most of 1988, until it reversed its stance in December. The banking authorities attempted to boost economic activity by holding interest rates down. Much of the increase in monetary aggregates, however, was concentrated in foreign currency balances held in Kuwaiti commercial banks, rather than in the broad Kuwaiti dinar denominated money supply. There also appeared to be a significant leakage of funds to Western financial markets as the low interest rates in Kuwait, combined with the absence of foreign exchange controls, opened up an incentive for borrowers to invest in foreign markets. The purpose of the relaxed monetary policy was to provide low-interest rate funding to spark local investment spending. However, investment spending in Kuwait has not been particularly responsive to interest rate changes in recent years. Fiscal policy has been more effective, especially since much of the investment opportunity has been in the government-dominated oil sector. While there was some expectation that the cease-fire in the Iran/Iraq war would touch off the resumption of the commercial reexport trade with Kuwait's neighbors to the north and east, results in the last half of 1988 gave no evidence of an upturn in the demand for inventory financing. The low-interest rate policy also made it easier for the government to continue financing its deficit by selling bonds and bills to the local market without a crowding-out effect on local businessmen seeking funds for investment in inventories or other investment.

By the end of 1988, it became clear that the low-interest rate policy was not meeting its principal objective. At the same time, the monetary authorities were witnessing increasing demands for foreign currency, which ultimately had to be supplied by the Central Bank, the residual supplier of foreign exchange under Kuwait's fixed exchange rate system.

The value of the Central Bank holdings of foreign assets declined from KD914 million at the end of 1987 to KD399 million by the end of the year. In December 1988, the monetary authorities reversed the direction of monetary policy by raising the interest rate ceiling on loans and linking the ceiling to the Central Bank discount rate. The move led to interest rates rising from an average of 6 to 7 percent to about 10 percent. Earlier in 1988, rates had been in the 3 to 4 percent range. The effect of the monetary policy change was a temporary reverse in the direction of flows between the domestic and foreign money markets, with an increase in KD-denominated time deposits. M2, for example, rose over KD450 million between the end of November 1988 and the end of February 1989 with most of the increase showing up as time deposits.

The Kuwaiti banking system benefits from a tradition of financial and trading activity by the leading commercial families. The banks have sought to modernize their operations, with widespread use of branch activities and Automated Transfer Machines (ATM) facilities. The Kuwaiti authorities would like to foster the country's prospects as a financial center for the region.

The Difficult Settlements Program: The Kuwaiti Government in mid-1986 adopted the Difficult Credit Facilities Settlement Program as a comprehensive approach to putting the banking industry back on its feet. Previously, the government had attempted piecemeal measures and isolated support programs for individual banks.

The program essentially calls for a rescheduling of outstanding debts to the banks over a 10 to 15 year period with the commercial banks, the Central Bank of Kuwait, and the debtors all making some sacrifices. The Central Bank concluded arrangements with most debtors and banks by the end of 1987, and the other Kuwaiti Government actions to formalize the agreements were completed for almost all the debts by the end of 1988. The Central Bank has provided support funds for the banks participating in the program.

The Exchange Rate and Foreign Exchange Reserves: The government officially follows a policy of fixing the exchange rate of the dinar against a basket of key currencies. The proportions of the weights in the basket are not published, but the relative importance of the currencies in the basket is said to be related to the role they play in financing Kuwait's foreign trade and payments. TWhen one of these currencies exchange rate changes the Dinar exchange rate is affected. For example, when the dollar declined against other major currencies during early 1988 the dinar strengthened against the dollar while declining against most other currencies. On the other hand, when the dollar began to appreciate in early 1989, the dinar sank against the dollar, while strengthening against currencies like the pound sterling or the deutschmark.

The relative movement of the dollar against other major currencies has an effect on the competitiveness of American goods and services in the Kuwaiti market.

Kuwait's official foreign exchange reserves, that is, those reserves held by the Central Bank of Kuwait and defined as reserves according to International Monetary Fund (IMF) practice, declined again in 1988. According to figures published by the IMF, reserves fell from $4.14 billion at the end of 1987 to $1.923 billion at the end of 1988. This figure is somewhat misleading as an indicator of the foreign exchange resources of Kuwait, since the Kuwaiti Government holds investment accounts abroad containing assets whose value is estimated at up to $80 billion. The Central Bank, however, does not have direct access to these funds, and its holdings are influenced by many factors, including the differential in interest rates between domestic markets and foreign markets.

Until the interest rate reform of December 1988, the easy money policy prevailing in the local market provided an incentive for local borrowers to obtain funds at low interest rates and, in the absence of foreign exchange controls, invest the funds abroad at a higher average interest rate. Since the exchange rate was fixed against a basket of currencies, the borrower did not run a major risk of losing interest income due to exchange rate effects. Since the Central Bank was the residual supplier of foreign exchange to the local market, it saw a substantial drawdown of its foreign reserve holdings as private sector borrowers took advantage of the interest rate and exchange rate policies. Some observers had suggested in previous years that the tensions caused by the Iran/Iraq war were the cause of the capital outflows from Kuwait. The continuation of the capital outflow after the Iran/Iraq cease-fire of August 1988 suggests that the outflow was due to economic incentives, that is, the interest rate differentials. With the increase in interest rates after December 1988, the Central Bank was able, temporarily at least, to halt the outflow of its reserves.

Investment: Domestic investment expenditure has been flat or declining since the early 1980s. There was apparently some upturn in domestic fixed investment in 1988, although levels still remain modest. The long Iran/Iraq war brought Kuwait's entrepot role to a halt, and inventories of tradeables fell. The cease-fire briefly revived hope that the reconstruction efforts to the north would renew Kuwait's transshipment activity. There have been few indications that much business has in fact resulted from the cease-fire, and inventories are being drawn down again by many establishments. Many Kuwaiti contracting firms had likewise looked for a renewal of activity. However, there has not been the kind of spending on contracting services in either Iraq or elsewhere in the area which these firms had expected; so spending on capital equipment for the construction industry has also not shown much of a change.

Kuwait has few local industries outside the oil sector and has not developed along the lines of a country with a trained local industrial labor force. Unless there is an upturn in economic activity in Kuwait's neighbors, it is unlikely that there will be an increase in capital spending to any significant degree.

The Kuwaiti Government and the private sector have remained very active as foreign investors. Kuwait has continued to run balance-of-payments surpluses on current account, with an estimated $4 billion to $6 billion available annually for capital investments abroad. The Kuwaiti Government follows a policy of diversifying its investment portfolio, with most of its investments over the past decade going to Western markets.

The Kuwait Investment Authority (KIA) manages the RFFG as well as Kuwait's State General Reserves. Neither the RFFG nor the State General Reserve are included in the Kuwaiti Central Bank holdings of foreign reserves. Since the KIA holdings are generally estimated at values in excess of $80 billion with a large proportion of the assets denominated in foreign currencies, KIA's total reserves far exceed those of the Central Bank. The KIA has a reputation for conservative financial management with much of its portfolio reportedly in dollar and yen investments. The Kuwait Investment Office, which is a related organization handling part of KIA's portfolio, came into some prominence in 1987 with the Kuwaiti purchase of a significant amount of British Petroleum Corporation (BP) shares in the London Market. After a dispute with the British Government over the proper size of its investment, the Kuwaiti Government reached a settlement with the British authorities in 1988 to reduce the Kuwaiti share of BP ownership to under 10 percent from the more than 20 percent share it had built up.

Estimates of total Kuwaiti private investment abroad vary widely, but some observers put the figure to half the size of official investment abroad. Therefore, although the figures are far from certain, it is clear that Kuwait has managed to build up a substantial stock of foreign assets in spite of a long period of recession and slow growth over the last decade. It remains a very wealthy country.

Inflation: The inflation rate in Kuwait showed little change in 1988, remaining at the low level of the previous several years. Even though the domestic economy has begun to expand, a number of factors have combined to keep demand from putting upward pressure on the price level. The foreign exchange regime tends to prevent importing inflation, and the availability of imports, along with stiff competition at the retail level, tends to preserve price stability. The Kuwaiti Government has also followed a policy of providing certain services such as medical care to the public for free or at reduced prices, which helps keep a lid on inflation.

If the economy continues its expansion, there may be some up-tick in the inflation rate, but it is unlikely that the rate will approach even the average of the inflation rates in the developed world in the next few years.

Population and Labor Force: Kuwait's Central Statistical Office estimated the Kuwaiti population at 1.958 million in mid-1988. Only 767,000 of this number were Kuwaitis, with the remaining 1.191 million long-term or short-term resident aliens who live in Kuwait for employment in the local labor and professional markets. Foreign workers make up more than 80 percent of the domestic labor market, according to consensus estimates.

Demographic policy in Kuwait has aimed at striking a better balance in the resident population between citizens and noncitizens, especially in the labor force. A number of proposals have been put forward to increase the number of Kuwaitis relative to foreigners in the work force, but the government has not yet decided on concrete proposals to achieve this goal. There is no unemployment in Kuwait, other than the frictional unemployment of workers moving from one job to another. Kuwaiti citizens can readily find work with the private sector or with the government, while expatriates who remain unemployed for any length of time lose their right to reside in Kuwait.

Balance of Payments: The Kuwaiti balance-of-payments current account remained in surplus in 1988. Although final figures have not been published on the components of the balance-of-payments accounts for 1988, the balance-of-trade surplus should have declined substantially from the previous year's value of over $3.5 billion. Lower prices for Kuwait's oil exports, combined with an increase in imports, have led to a decline of an estimated 50 percent in the merchandise surplus. On the other hand, Kuwait's investment earnings remain strong, and interest income remitted to Kuwait appears in the services account of the current balance. Although the Government of Kuwait was able to reinvest a good part of the earnings on its investments abroad, since it financed the deficit in the domestic budget by issuing government securities, the income from investment abroad should have contributed enough to maintain the current surplus in the $3 to $4 billion level. Capital outflows more than offset the current account surplus, however, and the Central Bank of Kuwait experienced a substantial drawdown in its foreign exchange reserves in 1988. By early 1989, the Central Bank holding of foreign reserves had fallen to under $2.0 billion, compared with $4.1 billion a year earlier. This outflow was mostly due to interest rate differentials between the Kuwaiti market and Western markets, especially in the months prior to the interest rate policy change of December 1988 in the Kuwaiti financial market. Kuwait continues to be an aid donor. The budget of the Kuwait Fund for Arab Economic Development supports an assistance level of around $300 million annually.

The Kuwait Fund provides development loan assistance to Arab and non-Arab developing countries and has been active in the foreign assistance field since 1962. The Kuwaiti Government, because of its own budget constraints, is no longer allocating support to the fund from its resources, but the fund can maintain its current level of annual programs by drawing on the earnings from its own reserves and from earnings on past loans.

PART B: THE PETROLEUM SECTOR

Production, Exports, and Revenues: Kuwait has proven oil reserves of over 90 billion barrels, second largest in the world. At current production levels of over 1 million barrels per day (b/d), the reserves would theoretically last for over a century, even if no new discoveries were made. All petroleum exploration, production, refining, and marketing is carried out by the government-owned Kuwait Petroleum Corporation (KPC) and its subsidiaries. The chairman of KPC is also the country's oil minister.

Since 1986, Kuwait's oil production levels have varied between 2.0 million b/d and less than 800,000 b/d, as KPC production levels fluctuated with market conditions and OPEC policies. Kuwait's OPEC production quota as of June 1989 is just under 1.1 million b/d, but Kuwait has made it clear that it will produce at a minimum 1.35 million b/d to meet existing requirements on its output. Kuwaiti leaders have said that Kuwait will maintain its commitments to long-term KPC customers as well as supply the KPC refining network and its overseas marketing network. Kuwait also has a share of the production from the Neutral Zone (also called the Divided Zone), which straddles the border between Kuwait and Saudi Arabia. The Kuwaiti share of Neutral Zone output is approximately 200,000 b/d. Kuwait exports crude oil and refined product from KPC facilities. The three KPC refineries located along the coast south of Kuwait City have a capacity of about 700,000 b/d, following the recent inauguration of the latest refinery at Mina Abdullah. Local consumption of refined products averages about 70,000 b/d, so Kuwaiti exports of oil will remain evenly divided between crude oil and product if exports remain at the 1.35 million b/d level. KPC markets about 250,000 b/d of product through its "Q-8" chain of gasoline stations and wholesale distributors in Western Europe. The chain may soon expand operations into the Far East as well. KPC also owns two refineries in Western Europe. Japan and other East Asian nations are Kuwait's main customers for crude oil exports, although KPC has begun making substantial sales in the North American market as well.

Since February 1987, Kuwait has set the official price for crude at $16.67 per barrel. Kuwait crude is a blend of crudes from various Kuwaiti fields.

Kuwait markets its crude at varying prices, according to market conditions. Likewise, its refined products and LPG exports are sold at market prices negotiated with buyers. The figures for oil export revenues in 1988 have not been published, but are expected to be in the range of $7 to $8 billion.

Domestic Developments: KPC has continued its search for nonassociated natural gas by drilling deep exploratory wells in several parts of the country, but has so far been unsuccessful in finding gas. KPC continued to develop the Marrat and Minagish reservoirs, two deposits of light, high-quality crude. The completion of the Mina Abdullah refinery brings to an end one of the largest refinery construction projects in the Middle East in recent years and has led to a drawdown of the large number of employees employed in Kuwait by its Santa Fe-Braun subsidiary.

Foreign Developments: Kuwait is the only major oil-producing nation to own its own retail sales and distribution network in a major market. While some other states have or are planning to enter into joint retail ventures with oil majors, KPC, through its Kuwait Petroleum International (KPI) subsidiary, has been in the retail market in Western Europe since 1983. At that time, KPC purchased 3000 gasoline stations of the Gulf Oil network in Western Europe. It markets its products through these stations and others it has purchased or built in Europe under the "Q-8" label. KPI has outlets in Britain, Italy, the Benelux countries, Denmark, and Sweden, and is contemplating expansion into the Far East. KPC's oil tanker subsidiary, the Kuwait Oil Tanker Company, has four very large product carriers (VLPCs) to supply KPI's network through KPC's Rotterdam loading terminal. Another KPC subsidiary, KUFPEC, the Kuwait Foreign Petroleum Exploration Co., has continued its oil exploration efforts outside Kuwait, with oil search activities concentrated mainly in the Arab World and the Far East.

Marine Transport: Kuwait uses tankers to transport its oil exports. During the latter years of the Iran/Iraq war, 11 tankers of the Kuwait Oil Tanker Company (KOTC) sailed under the American flag and received U.S. Navy protection. The protection kept Kuwait's oil export avenue open and guaranteed Western access to Kuwait's oil. Following the cease-fire, Kuwait and the United States have consulted closely about the status of the ships, and Kuwait decided to remove some of the ships from the American register while keeping five under the U.S. flag. KOTC also charters a number of tankers with the number varying according to market conditions. It has also decided to expand its fleet by building six new tankers.

PART C: IMPLICATIONS FOR U.S. BUSINESS

Commercial Outlook: Measures adopted by the Kuwaiti Government in recent years to resolve the banking sector's bad debt crisis caused by the Souk Al-Manakh stock market crash of the early 1980s and the recovery in the oil market have strengthened the economy. Government budget outlays also contributed to a second year of moderate economic growth. This growth should continue or increase slightly in 1989. If the dollar stays in a competitive range vis-a-vis major European currencies and the Japanese yen, prospects for U.S. exporters of goods and services will continue to improve.

With the Gulf war cease-fire in August 1988, many local businessmen expected an economic boom and hoped to recapture traditional reexport markets to Iran and Iraq. However, normal commercial relations with Iran have yet to resume, and trade with Iraq has been limited due to foreign exchange shortages. Until a peace treaty is signed, local businessmen and financial institutions will be unwilling to provide significant export financing. Even then, economic growth in the region is not likely to approach "boom" conditions.

Development Spending: Government spending remains the major engine of domestic business activity. Figures for the 1989/90 budget indicate that development spending will continue at current levels and will focus on social welfare projects with a high content of local goods and services. Spending will target essential services in the areas of housing, road construction, public utilities, education, telecommunications and medical care. There should be sufficient project variety and volume to attract international contractors; design, engineering and project management firms; and suppliers.

Major Projects: A complete list of all major project activity in Kuwait can be obtained from the U.S. & Foreign Commercial Service at the U.S. Embassy in Kuwait or from the respective desk officers at the Departments of State and Commerce. Projects now planned or under way include: the Kuwait Bay Causeway/Bridge; infrastructure to support F-18 aircraft; the Amiri Diwan office building, including offices for the Council of Ministers and the Crown Prince; headquarters for four government ministries; Kuwait University expansion; Sabiya power station; Shatt Al-Arab water conveyance; new sewer network; electrical grid interconnect among Gulf Cooperation Council States; and recarbonation systems for the water desalination units of all power stations.

U.S. Market Position: The Kuwaiti market will remain thin and highly competitive in line with the state of the economy. However, the U.S. market share is showing dramatic improvement as the impact of the U.S. dollar's decline works its way through the international economy. In 1988, U.S. exports to Kuwait increased 37 percent to $690.3 million. Unofficial partner country data during the same period show the value of

British exports to Kuwait up 12 percent, German exports unchanged, and Japanese exports down 15 percent. The United States is now very close to overtaking Japan as the leading export country to Kuwait. U.S. exports during the first three months of 1989 continued to increase. Prospects for continued growth will largely depend on the direction taken by exchange rates between the U.S. dollar and competitor country currencies. Traditional U.S. export strength has been in cars, trucks and spare parts; commercial aircraft; air conditioning and refrigeration equipment; industrial machinery including oil and gas-field equipment; services, and consumer goods.

Prospects for U.S. Business: The highly competitive local market is causing more and more Kuwaiti traders to look to the United States instead of traditional European or Japanese suppliers. But U.S. firms must still offer competitive prices and good service. U.S. firms should do well in areas where U.S. products and services have a technological edge and where U.S. expertise and brand names are respected. In addition to the traditional exports above, prospects are good for telecommunications, computer hardware and software products, safety and security systems, medical equipment, fashion apparel, foodstuffs, and other consumer products. Additional areas of interest include equipment and services in specialized fields such as waste treatment, environmental protection and alternative energy.

Arab Boycott Complications: Kuwaiti adherence to the Arab League boycott of Israel may prevent some U.S. firms from doing business in Kuwait. Some companies are already blacklisted. Others cannot bid on Kuwaiti Government tenders if under investigation by boycott authorities, but their goods may still be marketed through non-tender sales. At times, U.S. firms may be caught between conflicting requirements of Kuwaiti boycott and U.S. antiboycott regulations. Some of these conflicts can be resolved; others cannot.

U.S. firms encounter Kuwaiti boycott procedures in certificates of origin, letters of credit, shipping documents, government tenders, and in requests for information about a firm's business relationships. Generally, the receipt of a request to furnish information or otherwise participate in a restrictive trade practice or boycott must be reported to the U.S. Department of Commerce, although there are exceptions. For more guidance on boycott regulations or problems, U.S. firms should contact the U.S. Embassy Commercial Attache; the Office of Antiboycott Compliance, International Trade Administration, U.S. Department of Commerce, Washington, D.C, 20230, tel. (202) 377-2381; or the Office of General Counsel, U.S. Department of Treasury, tel. (202) 566-5569.

Getting into the Market: To penetrate the Kuwaiti market, a local agent or representative is usually required under Kuwaiti law. Local representation is essential for timely notification of major projects and tenders, and to maintain contact with ministry officials and decision-makers.

Use of the Department of Commerce Agent Distributor Service (ADS) is an excellent and inexpensive tool to establish initial contact with potential agents or distributors. However, the U.S. businessperson who makes periodic trips to Kuwait will be the most successful. The importance of direct contacts and personal relationships with Kuwaiti counterparts cannot be overemphasized.

Joint ventures with Kuwaiti firms are the best means for competing successfully for major project work. In addition, numerous private sector Kuwaitis have expressed interest in establishing joint ventures or licensing arrangements to produce goods locally to replace those which are now imported. Proposals range from the manufacture of breakfast cereals to chemical catalysts for the oil refining industry.

Advantages which can accrue to such ventures are management control and limited liability for the partners. Joint venture arrangements may be flexible enough to permit an apportionment of profits not necessarily confined to respective ownership shares. However, before any U.S. firm establishes a presence in Kuwait, it should seek professional advice in order to understand clearly the implications of Kuwaiti corporate tax law.

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Room 2036, HCHB
Washington, D.C. 20230
Tel: (202) 377-2515

- For upcoming trade promotion events (trade missions, catalog shows, etc.):

John Flannagan or Alan Sterling
Regional Export Development Office
Department of Commerce
Room 1510, HCHB
Washington, D.C. 20230
Tel: (202) 377-1209
Fax: (202) 377-5179

- For the current status of any major project:

Kamal Zaher, Commercial Specialist
U.S. Embassy Kuwait
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